FILE COPY

No. 279

Supreme Court of the United States

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

INDEX

	Page
Opinion Below	1
Jurisdiction	1
Question Presented	1
Statutes and Regulations Involved	2
Statement	2
Reasons for Granting the Writ	7
Conclusion	13
Appendix A	1a
Appendix B	9a

CITATIONS

Cases:

Atlantic Life Ins. Co. v. *Wolf*, 54 A. 2d 641, 642 (Mun. Ct. App. D.C. 1947)	10
Brewster v. *Gage*, 280 U.S. 327, 337	10
Cammarano v. *United States*, 358 U.S. 498, 510	9
Campbell v. *Great National Life Insurance Co.*, 219 F. 2d 693 (5th Cir. 1955)	11, 12
Deputy v. *du Pont*, 308 U.S. 488	10, 11
FPC v. *Panhandle Eastern Pipeline Company*, 337 U.S. 498	8
FTC v. *Bunte Brothers, Inc.*, 312 U.S. 349, 352	8
General American Life Insurance Company, 25 T.C. 1265, 1267 (1956)	6
Helvering v. *Griffiths*, 308 U.S. 39	9
Helvering v. *R. J. Reynolds Tobacco Company*, 306 U.S. 110	9
John Hancock Mutual Life Insurance Co., 10 B.T.A. 736, 738 (1928) acq. VII-2 Cum. Bull. 20	8
John Hancock Mutual Life Insurance Company v. *United States*, No. 59-243-M (D.C. Mass.)	3
Metropolitan Life Insurance Company v. *United States*, No. 79-59 Ct. Cls.	3
Northwestern Mutual Life Insurance Company v. *United States*, No. 57-C-73 (D.C.E.D. Wis.)	3
Old Colony R. Co. v. *Commissioner*, 284 U.S. 552	11
Prudential Insurance Company of America v. *United States*, No. 55-59, Ct. Cls.	3
Silver Homes, Inc. v. *Marx & Bensdorf, Inc.*, —— Tenn. ——, 333 S.W. 2d 810 (1960)	10

Page

Smithwick v. *Whitley*, 67 S.E. 914, 915 (N.C. 1910) 10
Spring City Foundry Co. v. *Commissioner*, 292 U.S. 182 10
United States v. *Childs*, 266 U.S. 304 10
United States v. *Leslie Salt Co.*, 350 U.S. 383 8
United States v. *Plesha*, 352 U.S. 202 10
Webb v. *Southern Trust Co.*, 11 S.W. 2d 988, 989 (Ky. 1928) 10
White v. *Winchester Country Club*, 315 U.S. 32, 41 8

Statutes:

Internal Revenue Code of 1939 § 201(e)(1) 2, 3
Internal Revenue Code of 1954 § 803(a)(2) 2, 3
Life Insurance Company Tax Act for 1955 6
Revenue Act of 1921 ..... 2, 3, 4, 5, 6, 7, 8, 9
Revenue Act of 1924 3
Revenue Act of 1926 3
Revenue Act of 1928 3
Revenue Act of 1932 3
Revenue Act of 1934 ..... 3, 4
Revenue Act of 1936 3
Revenue Act of 1938 3
28 U.S.C. § 1255(1) 1

Miscellaneous:

Bulletin "H" Bureau of Internal Revenue, April 9, 1921 ..... 5, 8
Rev. Rul. 55-12, 1955-1 Cum. Bull. 259 6
Rev. Rul. 57-198, 1957-1 Cum. Bull. 94 6
H. R. Rep. No. 1098, 84th Cong., 1st Sess., pp. 6, 11 9
H. R. Bill 8245 ..... 4, 5
Sen. Rep. No. 1571, 84th Cong., 2d Sess., p. 6 9
Treasury Regulations 62, Article 671 ..... 4, 5, 8
Treasury Regulations 65, Article 671 4
Treasury Regulations 69, Article 671 4
Treasury Regulations 74, Article 961 4
Treasury Regulations 77, Article 961 ..... 4, 8
Treasury Regulations 86 4

Supreme Court of the United States

OCTOBER TERM, 1960

No.

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE UNITED STATES, *Petitioner*,

v.

THE UNITED STATES, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

Petitioner prays that a Writ of Certiorari issue to review the judgment of the Court of Claims in the above-entitled case.

OPINION BELOW

The opinions in the Court of Claims (Appendix A, pp. 1a-9a) are reported at 181 F. Supp. 241.

JURISDICTION

The judgment of the Court of Claims was entered on March 2, 1960, (Appendix A, p. 6a). On May 24, 1960, the time for filing this petition was extended by the Chief Justice to and including July 30, 1960. The jurisdiction of this Court is invoked under 28 U.S.C. § 1255(1).

QUESTION PRESENTED

The question presented is whether the court below is in serious error and in conflict with the decisions

of this Court and the Court of Appeals for the Fifth Circuit in holding that penalty charges made for the privilege of prepaying an indebtedness fall within the statutory term "interest," notwithstanding contemporaneously adopted Treasury Regulations, thirty years of administrative practice, and explicit Congressional recognition, all to the contrary.

STATUTES AND REGULATIONS INVOLVED

Section 244(a) of the Revenue Act of 1921 (42 Stat. 261, Section 201(c)(1) of the Internal Revenue Code of 1939 (53 Stat. 1), and Section 803(a)(2) of the Internal Revenue Code of 1954 (68A Stat. 1) all provide that in the case "of a life insurance company the term 'gross income' means 'interest, dividends and rents.'" The complete text of these statutory provisions and the text of the Treasury Regulations promulgated thereunder are set forth in Appendix B, *infra*.

STATEMENT

For a great many years petitioner and other life insurance companies have treated as nontaxable, penalty charges received from borrowers for the privilege of anticipating due dates and amounts due under certain promissory notes and mortgages (R. 71 and 74), on the ground that such charges were not "interest" within the phrase "interest, dividends, and rents" —the only items of income taxable to life insurance companies under the Revenue Act of 1921 and successive statutes through 1954. These charges, which are not compensation for the use of money, represent consideration for the surrender or discharge of a valuable asset. After officially acquiescing in this view for over a generation, respondent, in 1957, for the first time, as-

serted a deficiency against petitioner for the taxable years 1950-1954 claiming that prepayment penalty charges fell within the statutory term "interest." After payment of the deficiency and the subsequent denial of its claim for refund thereof, petitioner brought suit in the Court of Claims. On March 2, 1960, the Court of Claims accepted respondent's contention, granted its motion for summary judgment, and ordered petitioner's claim dismissed. (R. 6a.)

The respondent's effort to expand the accepted meaning of a 30-year old statute and the Court of Claims' acquiescence in that effort took place against this background:[1] Prior to the Revenue Act of 1921, the gross income of all business corporations, including life insurance companies, consisted of income "derived from any source whatever." In the Revenue Act of 1921, however, the "gross income" of life insurance companies was limited to "interest, dividends and rents." This limited definition was reenacted by Congress nine times during the following 35 years.[2]

[1] There are presently pending in the federal courts at least four cases involving precisely the question presented here. Northwestern Mutual Life Insurance Company v. United States, No. 57-C-73 (D.C.E.D. Wis.); John Hancock Mutual Life Insurance Company v. United States, No. 59-243-M (D.C. Mass.); Metropolitan Life Insurance Company v. United States, No. 79-59, Ct. Cls.; and Prudential Insurance Company of America v. United States, No. 55-59, Ct. Cls. Moreover, since the taxable years 1950-1954 of many life insurance companies are still open, the issue is presented in either deficiency or refund status with respect to a large number of similarly situated taxpayers.

[2] The same statutory definition of the gross income of a life insurance company was reenacted by Congress as Section 244(a) of the Revenue Acts of 1924 and 1926 and as Section 202(a) of the Revenue Acts of 1928, 1932, 1934, 1936 and 1938. Subsequently the definition was incorported in the 1939 Code as Section 201(c) and in the 1954 Code as Section 803(a)(2).

Treasury Regulations 62, promulgated in 1922 shortly after the Revenue Act of 1921 was passed, defined the phrase "interest, dividends and rents" as follows:

> "Art. 671. Gross income of life insurance companies.—Net income in the case of life insurance companies is gross income from interest, dividends and rents less the deductions allowed by section 245. Gross income comprises items 25-34, inclusive, of the income page of the annual statement for life companies (edition of 1920) adopted by the National Convention of Insurance Commissioners . . . ."

During the following decade, the same provision was readopted by the Treasury on six different occasions as Article 671 of Regulations 65 and 69 and as Article 961 of Regulations 74 and 77.[3]

Six editions of the applicable Treasury Regulations thus defined the gross income of a life insurance company as comprising items 25-34, of the income page of the 1920 edition of the annual statement for life companies adopted by the National Convention of Insurance Commissioners. This annual statement for life companies, which was utilized by Congress in enacting the Revenue Act of 1921,[4] con-

---

[3] In Regulations 86 promulgated under the Revenue Act of 1934 the provision in question was omitted and from 1934 on, the statutory definition was not supplemented by regulations. Nothing in Regulations 86 rescinded the provision contained in the earlier regulations. The provision was merely deleted, and as a substitute therefor the statutory language was repeated.

[4] Congress explicitly used the Convention Edition form of annual statement in adopting the Senate floor amendment adding section 246 to the House bill, H.R. 8245, which became the Revenue Act of 1921. Section 246(b)(1) and (7), respectively, of H.R.

tains a comprehensive listing of the items of income derived from any source whatever. As above indicated, income of a life insurance company derived from any source whatever was taxable under revenue acts prior to the Revenue Act of 1921. The annual statement divides such items of taxable income into three general categories: the first covers premium income, items 25-34 cover specific types of interest, dividends and rents, and the balance of the items, 35-40, list miscellaneous income, "From other sources."

Because the Treasury Regulations included only "items 25-34" in the gross income of a life insurance company after 1921, "item 36", among others, was not included. In Bulletin "H", which the Commissioner published on April 9, 1921, with respect to the taxation of life insurance companies *prior* to the Revenue Act of 1921, "item 36" is defined as "Bonuses received for prepayment or extension of mortgage loans," which were explained as follows (R. 221):

> "When a payment is received by a company either for the privilege of extending a mortgage held by it, or for the privilege of paying the principal of such mortgage in advance, the payment received constitutes gain and should be included in gross income,"

After enactment of the 1921 Act, Regulations 62 were issued. As pointed out above, Art. 671 of those Regulations stated that only items 25-34 were included in gross income, thus specifically excluding item 36.

8245, as thus amended, defined "gross income" and "expenses incurred" (in the case of insurance companies other than life or mutual) with specific reference to "the annual statement approved by the National Convention of Insurance Commissioners."

In consonance with this authoritative interpretation of the relevant statute, the Treasury for three decades after the 1921 Act regarded prepayment charges as not taxable to life insurance companies. In the mid-twenties it appears that the interpretation was questioned and resolved short of litigation when the Internal Revenue Service rendered formal administrative decisions granting claims for refund on the ground that such charges were not taxable as interest under the Revenue Act of 1921.[5] The Service also had occasion to consider the tax consequences to the payor of such charges and ruled that they were not deductible as interest because they were not paid for the use of borrowed money.[6]

Finally, in the Life Insurance Company Tax Act for 1955, which is applicable only to taxable years "beginning after December 31, 1954," Congress elected to tax life insurance companies on "gross investment income" which it defined as "interest, dividends, rents and royalties" and income received from "the entering into of any . . . mortgage . . . from which the life insurance company derives interest, rents or royalties and . . . the alteration or termination" of such a mort-

[5] Such administrative determinations were made in 1927 on the basis of claims for refund for the taxable years 1921 and 1922 filed by The Prudential Life Insurance Company of America and John Hancock Mutual Life Insurance Company.

[6] Rev. Rul. 55-12, 1955-1 Cum. Bull. 259. While the ruling recognized these charges as "business expenses" in proper cases this was of no significance to the numerous taxpayers who paid such charges with respect to non-business indebtedness, e.g., residential mortgages. The Service subsequently found it expedient to revoke this ruling without analysis or explanation after the Tax Court accepted the same view as the court below. Rev. Rul. 57-198, 1957-1 Cum. Bull. 94, General American Life Insurance Company, 25 T.C. 1265, 1267 (1956).

gage. In other words, where before 1955 the statute had reached "gross income" which was limited to "interest, dividends and rents" in 1955 the statute was extended to "gross investment income" and specifically included both interest and penalty prepayment charges.

Nonetheless, the court below permitted the respondent to repudiate a position long and consistently held and applied to numerous taxpayers, discounted the fact that Congress clearly thought a change in the statute was necessary to achieve the result desired by respondent, rejected the traditional meaning of the term interest, and found, after all these years, that when Congress used the term "interest" in 1921 it intended to tax penalty prepayment charges.

REASONS FOR GRANTING THE WRIT

The decision of the court below, which involves an important question of Federal income tax law, is contrary to the interpretation of the relevant statute found in contemporaneously adopted Regulations and evidenced by long-standing administrative practice, and is in conflict with decisions of this Court and with a decision of the Court of Appeals for the Fifth Circuit.

(1) The Court of Claims concluded that penalty prepayment charges are comprehended within the statutory term "interest" because it believed that the "general object" of those who formulated the Revenue Act of 1921 was to include all "investment income" within the phrase "interest, dividends and rents." But the undisputable fact is that neither the statute nor the regulations mention "investment income." Rather, it is the "gross income" of a life insurance company which is subject to tax, and since 1921 that

term has been defined as "interest, dividends and rents, *and nothing else.*" *John Hancock Mutual Life Insurance Co.*, 10 B.T.A. 736, 738 (1928), *acq.* VII-2 Cum. Bull. 20. Respondent's formal acquiescence in the *John Hancock* opinion, and the specific exclusion of all other types of income by Regulations 62 through 77, are precisely the kind of long-standing administrative precedent that this Court has found controlling in *FTC* v. *Bunte Brothers, Inc.*, 312 U.S. 349, 352, and *FPC* v. *Panhandle Eastern Pipeline Company*, 337 U.S. 498, 513. A strikingly similar effort by the respondent to depart from a long-standing administrative interpretation of a revenue statute was rejected by this Court in *United States* v. *Leslie Salt Co.*, 350 U.S. 383, where Mr. Justice Harlan, speaking for a unanimous court, said (350 U.S. 396-397):

> "Against the Treasury's prior longstanding and consistent administrative interpretation its more recent *ad hoc* contention as to how the statute should be construed cannot stand. Moreover, that original interpretation has had both express and implied congressional acquiescence, through the 1918 amendment to the statute (*supra*, p. 391), which has ever since continued in effect, and through Congress having let the administrative interpretation remain undisturbed for so many years."

Moreover, Bulletin "H" and Treasury Regulations 62 were published contemporaneously with the Revenue Act of 1921 by the very people who must have been consulted in the drafting of the 1921 Act. This in itself gives the views expressed in these publications overriding significance in determining the intent of Congress in 1921. As this Court held in *White* v. *Winchester Country Club*, 315 U.S. 32, 41, "substan-

tially contemporaneous expressions of opinion are highly relevant and material evidence of the probable general understanding of the times and of the opinions of men who probably were active in the drafting of the statute. As such, they are entitled to serious consideration, independently alike of reenactments of the statute while it was in force on the books . . .."

The decision below totally ignores the reenactment of Section 244(a) of the Revenue Act of 1921 by Congress nine times during the ensuring 34 years, and the reaffirmation by respondent for over a decade of the regulations excluding prepayment charges. Where there has been but a single reenactment this Court has found it to be controlling: *Cammarano* v. *United States*, 358 U.S. 498, 510; *Helvering* v. *Griffiths*, 318 U.S. 371, 395; *Helvering* v. *R. J. Reynolds Tobacco Co.*, 306 U.S. 110, 116. Thus the decision below rests upon an unwarranted disregard of highly relevant legislative and administrative history. While the court showed awareness of portions of this history and specifically recognized "that it was the consistent and unchallenged practice of the plaintiff and other life insurance companies from 1921 to 1950 to exclude prepayment receipts from taxable income" (R. 144), it justified its action under the erroneous impression that there had been no "conscious decision" (R. 145) authorizing what had unquestionably taken place in the administration of the relevant statute. Its error may, therefore, be attributed to an unawareness of positive evidence of such a "conscious decision" which does in fact exist.

Nor did the court below accord the 1955 amendment of the statute proper significance. Both the Senate and House Reports in support of that amendment un-

equivocally state that the definition of income under prior law was being "expanded."[7] The decisions of this Court establish that even in the absence of such illuminating legislative history, "the deliberate selection of language so differing from that used in the prior acts indicates that a change in the law was intended." *Brewster* v. *Gage*, 280 U.S. 327, 337; *United States* v. *Plesha*, 352 U.S. 202; *Spring City Foundry Co.* v. *Commissioner*, 292 U.S. 182.

In sum, the decision below is so clearly erroneous, does such violence to one of the most important income tax concepts and so substantially and unfairly affects the nation's life insurance industry that it requires the certiorari attention of this Court.

(2) Moreover, the court below adopted a definition of interest that is inconsistent with the decisions of this Court.[8] A uniform meaning of "interest" is highly desirable inasmuch as the term appears in more than forty sections of the Internal Revenue Code.

The classic meaning of interest is "compensation for the use or forbearance of money." *United States* v. *Childs*, 266 U.S. 304; *Deputy* v. *du Pont*, 308 U.S. 488. In *du Pont*, the Court considered the question of whether carrying charges on short sales of stock

---

[7] H.R. Rep. No. 1098, 84th Cong., 1st Sess., pp. 6, 11; Sen. Rep. No. 1571, 84th Cong., 2d Sess., p. 6.

[8] It has been uniformly held that penalty charges imposed for the privilege of prepayment do not constitute interest within the meaning of usury statutes. *Silver Homes, Inc.* v. *Marx & Bensdorf, Inc.*, —— Tenn. ——, 333 S.W. 2nd 810 (1960); *Atlantic Life Ins. Co.* v. *Wolf*, 54 A. 2d 641, 642 (Mun. Ct. App. D.C. 1947); *Webb* v. *Southern Trust Co.*, 11 S.W. 2d 988, 989 (Ky. 1928); *Smithwick* v. *Whitley*, 67 S.E. 914, 915 (N.C. 1910).

could be regarded as interest paid or accrued, and held they could not, noting that the question had been early put to rest in *Old Colony R. Co.* v. *Commissioner*, 284 U.S. 552, where "interest" had been defined as

> "the amount which one has contracted to pay for the use of borrowed money. It there rejected the contention that it meant 'effective interest' . . . or that 'Congress used the word having in mind any concept other than the usual, ordinary and everyday meaning of the term.' It refused to assume that Congress used the term with reference to 'some esoteric concept derived from subtle and theoretic analysis.'" 308 U.S. at 497-98.

In the *du Pont* decision the Court pointedly refused to broaden that definition so as to include what it called "effective interest."

> "In the business world 'interest on indebtedness' means compensation for the use or forbearance of money. In absence of clear evidence to the contrary, we assume that Congress had used these words in that sense. In sum we cannot sacrifice the 'plain obvious and rational meaning' of the statute even for 'the exigency of a hard case.'" 308 U.S. at 498.

(3) The decision below also conflicts with that of the Court of Appeals for the Fifth Circuit in *Campbell* v. *Great National Life Insurance Company*, 219 F. 2d. 693 (5th Cir. 1955).[2] There respondent asserted that royalties were to be included within the gross income

[2] The *Great National* case is not mentioned or cited in the decision of the court below, although it was called to the court's attention in the briefs of both parties and was relied on by the petitioner on oral argument, and its relevance to this issue is not disputed.

of a life insurance company on the ground that royalties were in the nature of "rents" and hence within the definition of "gross income." Respondent argued there, as it must here, that Congress "in defining the gross income of life insurance companies as including 'rent,' clearly intended to encompass all forms of investment income described by that term in its broad generic sense and thus to include royalties." 219 F. 2d at 695.

The Court of Appeals found respondent's argument to be "without support in either the terminology or the theory of the statute." The court distinguished between rent, which by definition is fixed in amount regardless of the extent of the use of the property within a given period, and royalties, which are compensation based entirely upon the use actually made of the property.

> "By defining statutory gross income to include only interest, dividends, and rents, the intention was disclosed to omit all other factors from consideration. The statute is clear and unambiguous and we are constrained to apply it according to its tenor and terms." (219 F. 2d at 696)

The decision below clearly conflicts with the tenor and terms of the governing statute, the established administrative interpretation and practice, and the relevant case law.

CONCLUSION

For the foregoing reasons, petitioner prays that a writ of certiorari issue to review the decision of the Court of Claims and suggests that summary reversal would be appropriate.

Respectfully submitted,

JOHN LORD O'BRIAN
DANIEL M. GRIBBON
ROBERT L. RANDALL
701 Union Trust Building
Washington 5, D. C.
Attorneys for Petitioner

ROBERT L. HOGG
STUART MCCARTHY
393 Seventh Avenue
New York 1, New York

COVINGTON & BURLING
701 Union Trust Building
Washington 5, D. C.
Of Counsel